Governmental Regulation

of

Common Carriers by Railroad

An Address

Delivered Before The

Graduate School of Business Administration

of

Harvard University

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April 4, 1916

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*"Regulation is not intended to be a mere wanton exercise of power. It is a restriction upon the management of the railroads. It is induced by the public interest or safety."**

The railroad transportation plant of the United States comprises 250,000 miles of line, which with double tracks, yards and sidings, approximates 376,000 miles of track.

The capital securities, that is, the stock and funded debt of these companies, which were outstanding in the hands of the public on June 30, 1914, amounted to approximately $15,719,692,925,† of which probably sixty per cent. were bonds and other forms of indebtedness, and forty per cent. was stock, the latter being owned by over six hundred and twenty thousand stockholders. Insurance Companies with their thirty-four millions of policies outstanding, and Savings Banks with their ten million seven hundred thousand depositors, hold probably over ten per cent. of these securities.

* Per Mr. Justice McKenna in Erie R. R. vs. New York, 233 U. S. 671,683.

† Includes only railroads with annual operating revenues over $100,000.

During the year ending June 30, 1914, the operating revenues* of the railroads amounted to $3,047,019,908, their operating expenses to over $2,200,000,000 and their net operating income to $675,511,552, while the number of their employees for the year ending June 30, 1914, was 1,695,483,† and the compensation of such employees aggregated $1,373,422,472.

During the same period of time these Carriers paid in taxes over $140,000,000.

That the people of the United States have a vital interest in the efficiency of their system of railways is self evident. It is obviously essential to our welfare, economic and otherwise, that we have adequate railroad facilities, *i. e.,* sufficient track, stations, equipment and other facilities properly maintained and efficiently operated, and that the charges for the use of such facilities shall not only be nondiscriminatory, but shall also be just, reasonable and compensatory.

It is equally clear that sound public policy requires that there shall be governmental control and regulation of railroad charges, and possibly of other features of railroad transportation, and that such control should be exercised, not by statute laying down a hard and fast rule and affording no play to varying conditions, but through a body of experts, under a salary sufficient

* Includes only railroads with annual operating revenues over $100,000.

† The number of employees for the year ending June 30, 1913, was 1,813,289, and the reduction in number in 1914 was due to the decrease in business and rigid economies forced upon the railroads by their diminishing net income.

to attract men of the widest experience, and with such tenure of office as would render them free from political influence of any kind.

A fair example of another kind of regulation, *i. e.*, by statute, is found in the extra crew laws of the various States. The extra crew law makes the number of trainmen on a train depend solely upon the number of cars in the train, irrespective of the character of service performed by such train. For example; one of the usual types of this law requires a greater number of trainmen on trains consisting of four or more passenger coaches, and on freight trains of thirty or more cars, than is required by trains of a lesser number of cars, thus ignoring the fundamental consideration that the number of trainmen should depend not upon the number of cars but upon the character of the service performed by that train, whether through, or local, the amount of switching required, the conditions under which the switching is performed, and the differences in grade over which trains are run.*

Another example of vicious regulation by statute is the two-cent passenger fare law passed by many of the States, which ignores entirely the cost of the passenger service, and affords no opportunity for a proper increase in fare to take care of the large increases in the expenses of passenger transportation, which have taken place in recent years.

* See report of New Jersey Public Utility Commission, January 23, 1912.

It would seem clear also, that a body of experts necessary to efficiently carry out these processes of regulation, should be an administrative body, and not a Court.

The problems incidental to railroad regulations are essentially administrative, and not judicial, for they involve (as has been frequently pointed out by the Interstate Commerce Commission) not merely the respective interests of the complainant and of the defendant railroad company, but involve also the paramount interests of the community, which may be substantially affected by the controversy.

For example: A controversy between X, whose mine is located in the Pocahontas District in West Virginia, and the Norfolk & Western Railway Company serving that district, as to the rate to be charged on bituminous coal shipped from X's mine to Norfolk for subsequent transshipment by water, involves something more than the isolated question of the value to X of that transportation service and the reasonableness of the charge therefor.

Such a controversy, by reason of competitive conditions in the bituminous coal industry of the East involves amongst other things:

(a) Rates from all other mines on the Norfolk & Western Railway in the Pocahontas District to Norfolk, for transshipment by water.

(b) Rates from mines in the New River District on the Chesapeake & Ohio Railway and from mines

on the Virginian Railway to Newport News and Sewells Point, for transshipment by water.

(c) Rates from mines in the Cumberland-Piedmont, Myersdale, Austen-Newburg and Somerset Districts on the Baltimore & Ohio and on the Western Maryland Railroads in the States of West Virginia and Pennsylvania, to Baltimore and Philadelphia for transshipment.

(d) Rates from the mines on the Pennsylvania Railroad, New York Central Railroad, and Buffalo Rochester and Pittsburgh Railroad, in the Clearfield District in the State of Pennsylvania to Baltimore and Philadelphia for transshipment.

(e) The all-rail rates, from mines on the Baltimore & Ohio Railroad, Pennsylvania Railroad, New York Central, and Buffalo, Rochester & Pittsburgh Railway into New England.

This apparently simple controversy, therefore, between one coal company and the Norfolk & Western Railway Company, affects directly and indirectly the commercial prosperity of all the bituminous coal fields, from which bituminous coal is shipped to the East for local, coastwise, or export trade, and of all the large railroad systems engaged in that traffic,* and may also determine the extent to which coal traffic shall move through the competing ports of Norfolk, Lambert's

* This traffic is so large that its diversion would seriously affect the prosperity of some of these companies.

Point, Baltimore and Philadelphia for transshipment by water to New England.

Is such a controversy one which can properly be settled in a court of law, in a proceeding, in which the only necessary parties, would be X and the Norfolk & Western Railway Company?

A court of law is necessarily restricted, in the determination of an issue, to the evidence before it, together with the few facts of which a court may take judicial notice, and the court can only determine the issue, as presented by the parties.

As Mr. Acworth has pointed out,* railway questions are largely questions of discretion and commercial instinct, "and they are absolutely unsuitable for determination by the positive methods of the law court with its precisely defined issues, its sworn evidence, and its rigorous exclusion of what, while the lawyer describes it as irrelevant, is often the precise class of consideration which would determine one way or other the decision of the practical man of business."

An administrative body, on the other hand, can and should force the production of other evidence, and will consider the effect of their decision on other persons, and other localities, not parties to the proceeding, and is not hampered, therefore, by the lack of proof which may be presented by the contending parties.

* The Relation of Railroads to the State (page 12) by W. M. Acworth.

Our railways are national in character, that is to say, the direct and immediate effect of their activity is not confined to the locality or localities in which those activities may be exercised.

The commercial competition of points of production is such in this country, that the action of a railroad company in one portion of the country may seriously affect the economic development of another portion of the country. For example:

The competition between flour milled at Minneapolis, Kansas City, Chicago, Milwaukee, Buffalo and various points through Ohio and Indiana is of such a character that a change in the rates from one of those territories to the Atlantic Seaboard necessarily affects the ability of the other producing points to compete in the Eastern markets.

So, also, intra-state rates on raw material to important points of production, or rates on finished material to important points of consumption, may affect the ability of points of production in other States to compete in common markets.

State action making unduly low rates, freight or passenger, or State action unduly increasing the operating expenses of a railroad company, throws a direct and immediate burden* upon the entire traffic and operation of that company, which is reflected in its inability to properly serve the people in other

* See "The conflict between State and Federal Regulation of Railroads" by Walker D. Hines, published in the Annals of the American Academy of Political and Social Science for January, 1916.

States, or by compelling them to pay higher charges than they would otherwise be compelled to pay.

One of the primary reasons* for the adoption of our Federal Constitution was the burden imposed upon our commerce as a whole, by the conflicting regulations of the different States, and it was to eliminate that burden, that the exclusive power to regulate interstate commerce in matters of national concern, was taken away from the States and vested in the Congress of the United States.

One of the tests, which the Supreme Court of the United States has laid down, for the purpose of determining whether any subject of interstate commerce is of national concern is the answer to the question—does the subject require uniformity of treatment? If it does it is national in character, and as such can be only dealt with by the national legislative body.†

Railroad regulation is a subject which requires that, in its exercise, there shall be no discrimination in favor of the products or people of particular states, and that the body which is to enforce such regulation, shall have a broad comprehensive knowledge of the necessities and requirements of the entire country. It, therefore, follows that there must be uniformity of action, and such uniformity of action can only be secured through the medium of one central body responsible to the entire country, and not through

* Critical Period of American History (page 144) by James Fiske.
† Minnesota Rate Cases, 230 U. S. 352, 401, 402.

the medium of the representatives of 48 States, who are responsible only to their respective constituencies.

If then our governmental regulation is to be affected by and through an administrative body, what is to be the personnel of that body, and their tenure of office?

It will hardly be doubted that the problems incidental to railroad regulation are fundamentally difficult, and their proper solution calls not only for industry and intelligence, but also for the possession and exercise of that knowledge and imagination which can foresee the economic effect of the rate structure under consideration.

Let us assume that the administrative body has before it, the question as to the rates on coal, or ore, or limestone, to any of the iron furnace districts east of Chicago, or the rates on the finished product from such furnaces to the great competitive markets in the East.

The decision of this question might call for a consideration of the extent of the competition between Cleveland, the Mahoning and Shenango Valleys and Pittsburgh as points of manufacture, or the competition, if any, between the bee-hive coke manufactured in ovens in the Connellsville District in Pennsylvania, in the Pocohontas District in West Virginia and that produced in by-product ovens at other points. The Commission might have to consider the relative freight rates from the Atlantic Seaboard, on ore im-

ported from South America and Sweden, as compared with the rates on ore mined in the States of Minnesota and Wisconsin, and before they had finished their labors, they might be called on to remember that the furnaces in the States of Alabama and Tennessee, by reason of their cheap labor and their proximity to the sources of their supply of raw material, can and do ship pig iron to New England in competition with furnaces located at eastern points and in Northern New York.

The solution of such a question, might determine conclusively, the economic future of any of these points of production.

The Commission would also have to keep before them, the effect of the tonnage and the rates under consideration, upon the revenues of the carriers, for as the Interstate Commerce Commission said in the 1910 Rate Case (20 I. C. C., at pages 262, 263):

> "Our railroads must be maintained in a high state of efficiency. This the public interest demand. Commerce and industry cannot afford to wait on transportation facilities. Our rates should be such as to render possible a high-class, not an extravagant, service. * * *
>
> "It is generally conceded that within the next few years, if our means of transportation by rail are to keep pace with the calls upon them, very large sums must be expended in the way of new construction and new equipment. While some small portion of this may come from current earnings, the great bulk must be new capital, and this capital must be obtained from the investing public.

> "If, therefore, we are to rely in the future, as we have in the past, upon private enterprise and private capital for our railway transportation, the return must be such as will induce the investment. It is therefore not only a matter of justice, but in the truest public interest, that an adequate return should be allowed upon railway capital."

Our administrative body then must be composed of men of ability and foresight, with a thorough knowledge of the subject, and they must receive a compensation commensurate with their ability and responsibility.

Furthermore, their term of office must be of such length, as to make the position the life-work of the applicant, and thus remove the political influence incident to a short term of office.

As preliminary then to our discussion of the subject we will consider these propositions as settled:

(a) Public policy requires that there shall be efficient governmental regulation of common carriers by railroad.

(b) Efficient regulation requires a careful and exhaustive examination of the subject, by a trained body of experts, and accordingly no regulation by statute can be efficient.

(c) The questions incidental to regulation are largely administrative and are not judicial in their nature. They involve not simply the interest of the particular litigant in the particular issue, but they

necessarily affect other important issues and the interests of many persons and localities not parties to the controversy. They must be settled, in the first instance by an administrative body, and not by a court.

(d) The economic effects of the decisions of this administrative body or Commission, are so important and far-reaching, that the Commission must be composed of men who are making the subject their life study, and who shall receive adequate compensation for their services, and whose tenure of office shall be so long as to be entirely free from all political influence of any description.

(e) Railroad regulation fundamentally affects questions of national importance* which require uniformity of treatment. Such regulation should not be any more subject to State action, than our tariff, currency, or the operations of the Post Office Department.

Let us examine the present method of regulation, and see how far it conforms to the principles which have been outlined as a basis for efficiency.

As Mr. Samuel Rea, President of the Pennsylvania Railroad Company, said in his address to the Chamber of Commerce of New York on December 3, 1914: "The time is ripe for suggestions concerning constructive railroad regulation and policy," and it is

* See an address by Frank Trumbull entitled "Railway Service: Is it a National Problem or a Local Issue?"

upon the suggestions made by him at that time, that the views expressed in this paper are primarily based.

Governmental regulation, as at present constituted, involves the use of many regulating agencies, all operating at the same time upon such common carriers by railroad as come within their jurisdiction and as Mr. Acworth says:* "it is only to be regretted that the quantity of the law errs as much on the side of excess as its quality on the side of deficiency."

Those regulating agencies are:

(a) The Interstate Commerce Commission, acting under the authority of the Interstate Commerce Act, its amendments and supplements.

(b) Acts of Congress fixing compensation for carrying the mails.

(c) Action of Arbitration Commissioners under the terms of an Act of Congress.†

(d) State Public Service Commissions, operating under the terms of the Public Service laws of their respective States.

(e) Acts passed by State legislatures, establishing certain rates, freight and passenger, or prescribing operating conditions.

It may tend to clarity of discussion to consider these methods in the reverse order of their statement.

* The Relation of Railroads to the State by W. M. Acworth.
† Act of July 15, 1913.

I. ACTS PASSED BY STATE LEGISLATURES ESTABLISHING RATES, FREIGHT AND PASSENGER, OR PRESCRIBING OPERATING CONDITIONS

A. *State statutes establishing passenger and freight rates*

Examples of these statutes, so far as passenger fares are concerned, are the two-cent maximum fare laws of Minnesota, Ohio, Indiana, Illinois and West Virginia.

In freight cases, reference may be made to the Maximum Freight law of Minnesota (*Minnesota Rate Cases,* 230 U. S., 352), to the North Dakota Lignite Rate Law (*Northern Pacific vs. North Dakota,* 236 U. S., 585), and to the rates established by the State of North Carolina, under the Act of October 13, 1913, (*Royster Co. vs. R. R. Co.,* 38 I. C. C., 190).

As heretofore pointed out, the fundamental vice of the two-cent passenger fare law is, that the rates fixed thereby, do not bear the slightest relation to either the cost or value of the service.

This rate was fixed by the State Legislatures without the slightest examination into the cost of the passenger service, utterly ignoring the fact that a large portion of the passenger business (the commutation service) is being transacted at less than 2 cents a mile, and that the practical requirements of the commutation traffic would not permit its rates to be raised

to the maximum amount required by the statute. These statutes further ignored the fact that the cost of transporting passengers was increasing year by year, and thus operated to prevent the carrier from raising its passenger rates to meet the burden of such increase in costs.

That such costs have been increasing in recent years will appear from the opinion in the *"Five Per cent. Case"* where the Commission said (31 I. C. C., 351):

> "The unit of cost of moving certain kinds of bulk freight carried in large volume appears to have been reduced by more efficient operating methods despite increases in the rate of wages; on the other hand, the unit cost of moving passengers has been almost uniformly increased, independently of the effect of wage advances, through the use of heavier equipment, the adoption of safety devices, and better service." (Page 387.)
>
> "We know of no provision of law under which we should be justified in increasing freight rates to provide a return upon property used exclusively in the passenger service, much less to take care of losses incurred in such service. In our opinion each branch of the service should contribute its proper share of the cost of operation and of return upon the property devoted to the use of the public." (Page 392.)

In the *Western Passenger Case,* (37 I. C. C., 1), the Commission said (Page 41):

"The evidence in this case has shown:

"Substantial improvements in the passenger service have been made since 1900 at large expense to carriers, resulting in a greater degree of comfort, convenience, and safety to the traveling public.

"The conditions under which the passenger service is performed do not admit of all the corresponding economies in operation that have been effected in the freight service.

"The increased cost of service due to greater costs of labor, materials, and taxes not offset by corresponding economies which are practicable in operation, is entitled to consideration."

The Supreme Court of the United States in speaking of the two-cent fare law of one state said, (*Norfolk & Western Railway Co. vs. West Virginia,* 236 U. S., 605, 614):

"It is clear that by the reduction in rates the company is forced to carry passengers, if not at or below cost, at merely a nominal reward considering the value of the traffic affected."

It is also interesting to note that in some of the States in question, the Interstate Commerce Commission has permitted interstate rates to go into effect which are on a higher basis, than the rates fixed by the State statutes, and has also, in a litigated case, declined to recognize the rate fixed by the State statute, as evidence of the unreasonableness of the higher rate appli-

cable to interstate transportation in that locality. *Trier vs. Railway Company,* 30 I. C. C., 352.

So, also, in a recent case the Interstate Commerce Commission have declined to take freight rates fixed by the Minnesota statute as the measure of reasonable interstate rates in that State. *Holmes vs. Hallowell vs. Ry. Co.,* 37 I. C. C., 627.

Another example of State legislative freight rates, will be found in Chapter 51 of the laws of 1907 of the State of North Dakota, fixing maximum intrastate rates for the transportation of lignite coal.

The Supreme Court of that State found as a fact that as to one railroad company, the rate in question "is slightly remunerative, but in fact non-compensatory, considering the volume of freight carried and the property of the railroad devoted thereto." (26 North Dakota, page 439.)

As to another company that same Court found "that the carriage of lignite coal by the 'Soo' Line within this State during said fiscal year was not only non-profitable, but occasioned a loss to it when its fixed expenses apportionable to all traffic are in proper proportion, an amount assigned to and charged against the earnings from this commodity." (26 North Dakota, 439.)

The State insisted* that the statute could be supported as a matter of public policy in that it was to aid

* Nor. Pac. Ry. vs. North Dakota, 236 U. S. 585, 598.

in the development of a local industry, and thus confer a benefit upon the people of the State.

It may be sound public policy, to develop a particular industry, in a particular State. That is a matter for that State to decide, but no one will be heard to suggest that the people of one State should be taxed for the benefit of an industry located in another State. Yet that is the practical effect of State statutes which establish unremunerative freight and passenger rates, the loss to the carrier being shifted (at least in part) to the people and traffic of other States.

It has been estimated (*Five Per cent. Case,* 31 I. C. C., 351, 375), that the effect of the reduction in passenger fares in Ohio, Indiana, Michigan and Illinois by State statute was to cause a loss in revenues to ten of the carriers affected, of nearly $18,000,000 for the period between 1906 and 1913, which loss has imposed a burden either in rates or in impairment of service upon the traffic and people of other states.

B. *State legislation affecting operating conditions.*

In addition to the burden which has been imposed upon the people of the United States, by the passage of State laws prescribing maximum freight and passenger rates, there is also the economic injury inflicted upon the entire country by the passage of State laws regulating the details of railroad operation.

In the year 1913, 1395 bills, regulating the details of practical operation of railroads, were introduced in

the legislatures of the various States then in session. Two hundred and thirty of these bills were enacted into law. Amongst these laws were acts regulating the hours of service, time of payment, terms of employment of employees, rules for flagging trains, prescribing kind of headlight, equipment of passenger trains, speed of livestock and other freight trains, protection and elimination of grade crossings, equipment of all stations and shops.

In his recent and very convincing address on this subject, before the State Bar Association of Tennessee, Mr. Alfred P. Thom said:

> "Three States have passed laws making it illegal for a Carrier having repair shops in such State to send any of its equipment which it is possible to repair there, out of the State. Fifteen States have attempted to secure preferential treatment of their State traffic by heavy penalties for delay in movement. Twenty States have extra crew laws. Twenty-eight States have headlight laws with varying requirements as to character of lights."

In the year 1915 there were introduced in the State Legislature then in session, 1097 bills directly regulating railroad operation, of which 137 were enacted into law. Amongst those enacted into law were bills regulating the size of crews, the hours of service, the character of headlights and other appliances on equipment, the speed of freight trains, the stops of

passenger trains, the installation of signals, elimination of grade crossings, the location of stations, etc.*

It will hardly be contended that a legislative body has or can acquire the technical knowledge necessary to enact legislation of this kind. The most scientific method of regulating (if the subject be one which requires regulation) such matters, would seem to be by action by a Commission after a careful investigation of the facts, an investigation which cannot be made by a legislature, on account of other necessary demands upon its time.

Indeed, many of the States which enacted the laws referred to, possessed Public Service Commissions with ample power to deal with the situations covered by the bills.

But careful investigation of the subject, by a body of experts, is not desired by the interests which seek the passage of laws of this character.

In 1911 the Public Utility Commission of New Jersey was directed by the Senate of that State to advise as to the propriety of the passage by the Legislature of an extra crew law.

After a careful consideration and hearings, at which the labor organizations were fully represented, that Commission on January 25, 1912, advised the Senate, that in the opinion of the Commission the Bill should not be passed as it was defective and

* "Railroad Regulation in Illinois," by Blewett Lee, 10 Ill. Law Review, page 402.

erroneous in principle, and that the extra cost to the companies was a public and social waste.

Notwithstanding this report, the Legislature of New Jersey subsequently passed an Extra Crew Law. One example of the operation of this law, was to require one of the railroad companies to employ an additional brakeman upon a through passenger train, which made only one stop in the State of New Jersey, and which train already carried four railroad employees, and seventeen mail, dining car, and Pullman employees, or twenty-one in all. This statute and a similar one in Pennsylvania, cost the railroads in those two States, $1,721,327.91 during the calendar year 1914, an absolute economic waste.

Legislation of this character is, as Governor Hughes pointed out in his veto of the bill in the State of New York, "simply arbitrary exaction and taking of property without due process of law."

Wasteful and injurious as is the extra crew law to the public interest, it is but slight as compared to the maximum train law, which has been enacted in one State, and the passage of which is being continuously urged in many States.

This law limits the number of cars to a train, thereby increasing the number of trains, and like the extra crew law, its fundamental object, is the employment of unnecessary men, with the consequent economic waste.

As you know, railroad companies during the last fifteen years have been spending large sums of

money in the construction of larger and heavier cars and more powerful locomotives, for the purpose of increasing the average loading per car, as well as the average number of cars per train, and thus effecting a reduction in freight train mileage, with the consequent saving in operating expense.

The use of this larger and heavier equipment has necessitated (as the Commission pointed out in the *Five Per cent. Case,* 31 I. C. C., 351, at page 377) heavier rails, stronger bridges, better ballast, more ties, reduction in grades and elimination of curves.

Enormous expenditures have been made for the purpose of increasing the train loading, and the efforts of the Carriers in this respect have been declared by the Commission to be "great advances in efficiency" (31 I. C. C., at page 411). This efficiency which has resulted in the saving of expense, will be curtailed by a law limiting the number of freight cars on a train, thus forcing an increase in the number of trains and number of employees.

The plea of those who urge the enactment of maximum train and extra crew laws is safety. The real reason is to force the employment of additional and unnecessary men. So far as the writer knows, no accident has ever happened which would have been prevented by the passage of either of these laws.

In the trial of the Extra Crew Case in the State of Pennsylvania, it was a significant fact that the labor organizations, with their hosts of witnesses

of many years experience, could not and did not produce one single instance of an accident to passengers or employees, due to the failure to have the train crew prescribed by the Act. The same point was emphasized by the Board of Public Utility Commissioners of New Jersey, when they said:* "The Board believes it to be extremely significant that at the two public hearings the advocates of this measure, or one similiar to it, were unable to cite, when challenged, any serious accident resulting from the employment of insufficient train crews."†

One more example of the character and economic value of legislation of this kind.

It has been the practice for many years for many railroad companies to make surprise tests from time to time, as to whether their employees are obeying the signals. As a matter of fact, those tests show that those signals are obeyed in more than 99 per cent. of the cases.

In order to prevent, however, the disciplining of the men who fail to stand the test, a bill has been introduced in one, if not more than one State Legislature, making it a criminal offense to make a test of this kind without giving prior notice to the employee.

The passage of a law of this kind would be a direct menace to the safety of the traveling public.

* Report of the Public Utility Commission to the Senate, January 23, 1912.

† The people of Missouri in a recent referendum declined to enact an extra crew law.

As in the case of State legislation fixing freight and passenger rates, the economic waste resulting from extra crew, maximum train laws and other laws of this character is and will be borne in part, by the people and traffic of other States. No sound argument can be advanced in favor of any State statute regulating the details of operation.

II. STATE PUBLIC SERVICE COMMISSIONS

Regulation by State Commission of intra-state rates and practices affecting such rates, as well as of operating conditions, has so far proceeded that nearly every State has a Commission, with complete power to prescribe intra-state rates and practices, as well as operating conditions, such as the number and schedules of trains, character of equipment, construction and location of stations, etc.

Regulation by State Commission is, of course, based on a far sounder principle than regulation by State statute, but public policy now demands that the State Commissions be divested of jurisdiction over intra-state rates and that such jurisdiction be vested in the Federal Government. The reasons for this statement are as follows:

(a) State rates directly affect interstate rates.

The route of the New York Central between Buffalo and New York City is intra-state. The routes of the Pennsylvania Railroad, the Erie Railroad, the Lehigh Valley Railroad, and the Delaware, Lackawanna & Western Railroad Companies between those same points are interstate. If the New York Public Service Commission should reduce the rate on any article from Buffalo to New York via the lines of the New York Central, it is obvious that such reduction will, for competitive reasons, and to put shippers and consignees on the lines of the other roads on a competitive equality with the New York Central, force a corresponding reduction of the rates on the Pennsylvania and the other interstate routes.

Following the first opinion of the Interstate Commerce Commission in the Industrial Railways Case, 29 I. C. C. 212, the Trunk Lines canceled their allowances to the South Buffalo Railroad Company, owned by the Lackawanna Steel Company at Buffalo, thus forcing shippers, located on the South Buffalo Railway, to pay the 10-cent charge of the South Buffalo Railway in addition to the freight rate of the Trunk Line. The New York Commission forced the New York Central to reinstate their allowances to the South Buffalo Railway, on the intra-state route. The effect of this action was, that until the Interstate Commerce Commission permit-

ted the carriers to reinstate the allowances on the interstate routes, shipments originating on the South Buffalo Railway naturally went by the New York Central, as the rate was 10 cents less than the rate via the other routes. Similar action on the part of the Pennsylvania State Commission, in connection with the allowances paid the Union Railroad at Pittsburgh, necessarily accorded an advantage to consignees located in Philadelphia on the Pennsylvania Railroad, whose route is intra-state between Pittsburgh and Philadelphia, as compared with consignees located on the Baltimore & Ohio in Philadelphia, whose route from Pittsburgh is interstate.

As Mr. Justice Hughes said in the Shreveport Case, 234 U. S., at page 351:

> "Wherever the interstate and intra-state transactions of carriers are so related that the government of one involves the control of the other, it is Congress, and not the State, that is entitled to prescribe the final and dominate rule, or otherwise Congress would be denied the exercise of its constitutional authority, and the State, and not the Nation, would be supreme within the national field."

The rates established by the State of Minnesota which were under consideration in the Minnesota Rate Case, 230 U. S. 352, by reason of competition, have directly forced reductions in many inter-

state rates. (Holmes and Hallowell vs. Ry. Co., 37 I. C. C. 627.)

So, also, intra-state rates directly affect interstate rates, owing to the provisions of Section 4 of the Interstate Commerce Act, which prohibits the through rate from exceeding the sum of the local rates. (See Through Rates to Points in Louisiana, 38 I. C. C. 153.)

So, also, in a recent case (Western Rate Advance Case, 35 I. C. C. 497) the carriers were refused permission to advance certain interstate rates, apparently (see pages 589, 668, 669) upon the ground of the much lower basis in effect for intra-state rates.

Other examples of intra-state rates directly affecting interstate rates will be found in R. R. Com. of La. vs. Ry. Co., 23 I. C. C. 31; McCormick vs. Ry. Co., 37 I. C. C. 234; Texarkana Freight Bureau vs. R. R. Co., 38 I. C. C. 55; The Five Per cent. Case, 31 I. C. C. 351, 387; F. S. Royster vs. R. R. Co., 38 I. C. C. 190; Houston Ry. Co. vs. U. S., 234 U. S. 342.

(b) At least one State Commission, has frankly adopted a policy of protecting their own industries against the competition of industries of other States, by the adjustment of intra-state rates, and are thus, through this medium, accomplishing the commercial discrimination which the Constitution of the United States was designed to prevent.

Examples of State action, of this character, will be found in R. R. Com. vs. Ry. Co., 23 I. C. C. 31; Houston Ry. Co. vs. U. C., 234 U. S. 342, and McCormick vs. Ry. Co., 37 I. C. C. 234, and it violates one of the fundamental requirements of our system of government, viz., that

> "Interstate trade was not left (by the Constitution) to be destroyed or impeded by the rivalries of local governments."*

(c) As heretofore pointed out, the depletion of the revenues of the carriers resulting from unjustly low rates made by State Commissions, must be made up, by the rates on interstate traffic and the traffic of other States.

Notwithstanding the findings of the Interstate Commerce Commission, in the Five Per cent. Case, as to the inadequacy of existing passenger rates (supra, pages 14, 15), the action of one of the State Commissions, in suspending up to this time, the increase of the intra-state rates in that State, has not only prevented the increase of such rates, but has to a large extent prevented the railroad companies from receiving the increase on interstate rates permitted by the Interstate Commerce, because the interstate rates may be defeated by purchasing tickets at intra-state stations.

Under existing law, the Interstate Commerce Commission has the power to deal with a discrim-

* Per Mr. Justice Hughes in the Shreveport Case, 234 U. S., at page 350.

ination against interstate traffic resulting from intra-state rates (Houston Railway Co. vs. U. S., 234 U. S. 342), but it is probable that the State rates are valid (so far as this question is concerned), no matter how discriminatory they may be, until the Interstate Commerce Commission has specifically passed upon the question of discrimination. Minnesota Rate Case, 230, U. S. 352).*

If we are to have that uniformity of rate regulation, and that prevention of discrimination against localities, and the commerce of other states, which is so essential to our commercial development, and which the commerce clause of the Constitution was designed to secure, we must have State control divested from intra-state rates.

In Canada, a railroad operating in two or more provinces, is subject to the Dominion Parliament, and the Railroad Commission created thereby, and is not subject to the Provincial Legislatures.†

It will hardly be contended that the commerce of Canada, is more interdependent than the commerce of the United States, so far as the necessity of uniformity of rate regulation is concerned.

State Control Over the Issue of Railroad Securities

At the present time the Interstate Commerce Commission has no jurisdiction over the issue or

* See Federal Control of Interstate Railroad Rates by Henry W. Biklé in the University of Pennsylvania Law Review for December 1914.

† "Railroad Regulation in Illinois and Elsewhere," by Blewett Lee, 10 Ill. Law Review, page 402.

sale of securities. Some of the State Commissions have that jurisdiction, and many railroad companies are required to obtain the consent of the State Commission of one, or of sometimes more than one State.

The unavoidable delay and conflicting regulations and procedure, incident to securing the consent of more than one Commission, must inevitably, in many instances, seriously affect the price at which the necessary capital can be secured.

Without meaning to intimate that the following, is other than an isolated instance, the annual report of the Southern Pacific Railway Company contains this statement:

> "To provide funds for corporative purposes, arrangements were made with bankers, in May, 1913, for sale of two-year notes at a very satisfactory price. Authority of the California Railroad Commission to issue the notes was obtained without delay; approval by the Arizona Corporation Commission, however was withheld, pending certain assurances and guaranties on the part of the Company with reference to the conduct of its business in Arizona which it was not warranted in giving and, during the time the matter was pending before the Commission, the condition of the money market had so changed that a sale of the notes could not be made. Further consideration of a two-year note issue was abandoned, and one-year notes were issued instead, and

sold at a price yielding approximately $275,000 less than would have been received had the two-year notes been issued without delay. Under the laws of California and Arizona the issue of one-year notes did not require Commission approval."

Mr. Blewett Lee (in his interesting paper before referred to) points out how one State by a provision in its public utilities law, has been enabled to exact large sums of money from railroad companies incorporated under the law of that State, for permission to issue bonds, much of the proceeds of which are to be used for improvements in other States.*

All power with respect to the issue or sale of railway securities should be taken away from the States,† and be vested in the Interstate Commerce Commission to the extent and in the manner hereinafter indicated.

State Control of Railroad Operating Conditions.

It can hardly be doubted, but that, in the interest of economy and efficiency, there must be the same uniformity in the exercise of the power of regulating operating conditions, as in establishing and regulating rates.

* If there had been similar legislation in other States through which one of our large railroad systems runs, that company, would have been obliged to pay to the states, nearly the entire capital received under a recent loan.

† See recent report of the Massachusetts Public Service Commission on the New York, New Haven and Hartford Railroad Company.

Economy and efficiency does not permit, in the case of a railroad running through two or more States, of varying regulations in those States as to the character of safety appliances and equipment, hours of labor, character of headlight, etc. Furthermore, operating regulations of State Commissions, like State laws, may substantially increase operating expenses and thus ultimately affect interstate revenues and rates. Certainly such subjects as signals, number of trainmen, length of trains, character of road-bed and equipment, should be as completely removed from the jurisdiction of the States as have the questions of safety appliances, and the hours of service of employees, by the action of Congress. (*Ry. Co. vs. U. S.* 222. *U. S.*, 20; *Ry. Co. vs. Washington*, 222 *U. S.*, 370; *Erie R. R. Co. vs. New York*, 233 *U. S.*, 671.)

Divesting State commissions of jurisdiction over the rates and operating conditions of railroads, does not mean the abolition of State Public Utility Commissions. There remains an ample field for their jurisdiction, in the case of public utilities, not subject to the Interstate Commerce Act.

There is another feature, incident to State Commission regulation of railroads, which operates against the efficiency of such regulation. No one can view without concern, the increasing tendency, to consider the appointments to that position as purely political. It can hardly be anything but disheartening to a conscientious commissioner to feel that his appointment

does not depend upon his efficiency, but upon the political exigencies of the moment.*

The position requires industry, conscientious ability, and faithful service. Many members of the State Commissions possess these attributes, but their method of selection or election, tends more and more, to disregard each and all of these features.

III. ACTION OF ARBITRATION COMMISSIONS UNDER THE TERMS OF THE ACT OF CONGRESS OF JULY 15, 1913

As you are doubtless aware, wage disputes between railroads and their employees, may be settled by voluntary arbitration by arbitrators appointed under the terms of the Act of Congress of July 15, 1913.

When you remember that during the year ending June 30, 1914, the number of employees was 1,695,483, and their compensation aggregated $1,373, 422,472, it can readily be seen that the decisions of the arbitrators may substantially affect the revenues of the Carriers. How important those various increases in wages are may be seen from the fact that in the case of 30 of the 35 Eastern railway systems, if the scale of wages for 1909 had been in effect during 1913, the labor costs, of the latter year, would have been less by fifty-one millions of dollars, than they actually were.†

* In twenty-two States, the Commissions are elected. See "The Government and the Railroads," by Otto H. Kahn in the *World's Work,* February, 1916.

† The Five Per cent. Case, 31 I. C. C., at page 379.

In 1914, the last year for which the figures are available, wages were approximately 62.4 per cent. of the operating expenses (exclusive of taxes), and 45 per cent. of the operating revenues.

Notwithstanding the necessary relation between passenger and freight rates of the Carriers, and the wages paid their employees, the Act of Congress does not provide for the representation by the Interstate Commerce Commission in the arbitration proceedings under the Act, and we have had, therefore, in the past, decisions by arbitrators, increasing wages, without the slightest responsibility on the part of the arbitrators, with respect to the rates necessary to secure the funds to provide for such increases.

Thus in the 1913 Arbitration between the Eastern Railways and the Order of Railway Conductors and Brotherhood of Railroad Trainmen, the report of the Arbitrators, in granting the increase said (page 29):

> "The Interstate Commerce Commission, and not this Arbitration Board, has the duty ot determining whether the railroads can earn in addition to their other charges, without an increase in freight rates, the rates of pay that this Board believes to be due at the present time to the conductors and trainmen, which rates are embodied in the Award following."

The question of whether the rate of wage should be fixed, irrespective of the then financial ability of the carrier to pay the same, is not the question. No

matter how the wage may be fixed it must ultimately be paid out of operating revenues, *i. e.,* the receipts from the transportation of passengers and freight, which in turn depend upon the size of the passenger and freight rates.

There is, therefore, an intimate and direct connection between the wage and the transportation rate, and the public is interested in both.

It is hardly probable that the same economies can be expected in the future, to the extent that they have been obtained in the past, by increase in the capacity of the transportation units. Many of the improvements of the future, such as elimination of grade crossings, installation of automatic signals, enlargement and beautification of stations, etc., will be financially unremunerative.

It therefore follows, that any future increases in wages, will have to be paid for (in large part) out of increases in freight and passenger rates, and not out of operating economies. This being so, the body which has ultimate control of the rates, should participate in the deliberations of the Board of Arbitrators, and thus remove the present anomaly, under which, the agency which grants the increase in wages, has not the slightest responsibility with respect to the fund out of which the wages are to be paid.

The public interest demands, also, another change in the scope of the arbitrations. In the past,* the

* This is not owing to any defect in the Arbitration Act, but to the nature of the controversies, which have been presented for arbitration.

arbitrations have been entirely one sided, that is to say, the employees present certain demands, and the question arbitrated is, whether those demands, or some modification thereof, shall be granted. The employees have nothing to lose under this method, and by the simple process of making their demands high enough in the first instance, they may obtain, through a compromise, all they originally expected.

There are various rules and regulations, which from time to time the labor organizations of employees in the train service have forced upon the carriers. As to many of these there are grave doubts as to whether their existence is compatible with the public welfare. For example:

(a) If an employee's schedule of pay calls for 10 hours, or 100 miles, and he makes his run in 4 hours, or runs only 90 miles, he is not obliged to do any more work under the existing regulation.

(b) In various instances the men are paid twice for performing the same work. They are guaranteed their mileage or the hours, which ever is the greater, and in addition, if at the end of a freight run, they are required to switch a car of stock to a stock yard or perishable freight to a team track or warehouse, additional compensation is allowed, notwithstanding the time consumed in doing such additional work is included in the regular hours. They secure this allowance whether overtime accrues or not.

(c) The present rules provide for a guarantee of daily pay, though the man may only do 10 minutes work on a "run" for which he is called.

Under those circumstances the Company should have the right to call the employee for another run.

May it not be doubted whether rules of this character are compatible with efficiency and economy, and any arbitration of a demand for an increase in wages should involve also an arbitration of the demand on the part of the Companies, for an abrogation of these and similar rules.

IV. ACTS OF CONGRESS FIXING COMPENSATION FOR CARRYING THE MAIL (INCLUDING THE PARCELS POST)

Under existing law, the Railroad Companies are paid for the transportation of mail (including the Parcels Post), under a schedule of rates prescribed by the Act of Congress of March 3, 1873, which rates were reduced by the Act of July 12, 1876, and further reduced by the Acts of July 17, 1878, and March 2, 1907.

Rates established by this method are open to the same objections as rates fixed by State laws, and the rates named in the statutes bear no direct or adequate relation to the cost or value of the service.

The Carriers believe that the rates in question are unjustly low and in support of their belief show:

(a) That the rates are based, 90% on the weight of the mail transported and 10% on Railway Post

Office Cars for sorting mails in transit. The weight is obtained by weighings of the mail (carried by each Carrier) for ninety days once every four years. As the mail increases from time to time, the Railroads are underpaid (even under the rates fixed by the Act), for all mail transported during the period subsequent to the date of weighing and until the next weighing takes place.

(b) A joint Committee, (of which Senator Bourne was Chairman) of the Senate and House of the Sixty-third Congress, appointed to investigate the questions relating to the Railway Mail Pay, reported under date of August 31, 1914, that the Railroads were underpaid at least Three Millions of Dollars per year.

(c) Mr. Robert H. Turner, Secretary of the Committee, reported that the Railroads were underpaid approximately Twelve Millions of Dollars per year (Railway Mail Pay Hearings, page 962), and Mr. M. O. Lorenz, Associate Statistician of the Interstate Commerce Commission said that he thought there was an underpayment of at least 10 per cent. (or $5,000,000), although he recommended a further test of his conclusions. (Railway Mail Pay Hearings, page 894.)

(d) The Committee on Postal Affairs of the Merchants Association of New York, under date of October 21, 1915, (page 17 of the report), advised the Association, that the Railroads now underpaid for mail carriage, to the extent of approximately Eleven or Twelve Millions of Dollars per year.

(e) The Congressional Committee before referred to, reported (Appendix, pages 33-39) that during the years 1909-1910, the mail traffic earnings were, per car mile, 22 per cent. less than the passenger traffic earnings, and slightly over 20 per cent. less than the average earnings of the entire passenger service, which, as you will remember, the Interstate Commerce Commission in the Five Per cent. Case (31 I. C. C., 387-392) found were less than they should be.

(f) Mr. Louis D. Brandeis, Special Counsel for the Interstate Commerce Commission in the Five Per cent. Case, said, in his brief in that case (page 133), after discussing the evidence submitted to the Bourne Committee: "It seems clear that the Railway Mail service is at present unremunerative to the Carriers."

(g) A joint Congressional Committee reported in January, 1901, that the Railroads were not then overpaid. During the period 1900-1915, total receipts of the Post Office Department increased 181 per cent., total expenses increased 177 per cent., while the amount paid the Railroads for carrying the mail only increased 60 per cent. During that same period all expenses, except Railway Mail Pay, increased 239 per cent.

The scientific and equitable method of determining the question of proper compensation, is that urged by the Carriers upon Congress, viz., that the Interstate Commerce Commission should be given jurisdiction to pass upon the question.

V. REGULATION BY THE INTERSTATE COMMERCE COMMISSION UNDER THE PROVISIONS OF THE INTERSTATE COMMERCE ACT

If what has been said heretofore, with respect to railroad regulation, through State agencies and directly by Act of Congress, be correct, it follows that the necessary Governmental regulatory power should be exercised through a Federal Commission with sufficient numbers and proper personnel, and with such powers as may be necessary to accomplish efficient regulation. To accomplish these propositions, it is suggested:

(a) That the membership of the Commission should be materially increased, and the additional members of the Commission should be selected from men having broad experience in railroad management, operation, traffic and finance.

During the year 1915,* 964 formal complaints were filed with the Commission, 902 decisions rendered, and 205 cases dismissed by stipulation. 200,000 pages of testimony were taken, and 198 cases were orally argued before the Commission, 103 days being devoted to this latter purpose. As it was obviously impossible for the Commission (now composed of seven members) to devote 103 days to argument, and at the same time take 200,000 pages of testimony, the latter was taken chiefly before 45 examiners.

* See Annual Report of the Commission for 1915.

The Commission, also, during this period, conducted four investigations, pursuant to resolutions of Congress, as well as a large number of investigations instituted upon their own motion.

The Commission also disposed of 210 applications to suspend tariffs, entered 822 orders for relief from the operation of the Fourth Section of the Act, exercised the necessary supervision over the accounts of the Carriers, enforced the Safety Appliance and Hours of Service Law, and exercised their powers over Express, Telegraph and Telephone Companies. In addition to this work the Commission are responsible for the valuation of 250,000 miles of railroad and the property of telegraph, telephone, express companies, pipe line companies, and other common carriers subject to the Act.

This inordinate press of business has prevented some matters, from receiving the personal attention of the Commission, which the importance of the subject requires, and has necessitated their delegation to subordinates. This is a distinct element of weakness in the present system, and is likely to increase if not promptly remedied.

There is also in some instances, a distinct waste of time involved in the present method of taking testimony before the Examiners, and too much time has to be devoted by officers of carriers in attendance at these hearings.

As Commissioner Harlan has said in the *Western Advance Rate Case,* (35 I. C. C., 497, 681):

> "Too much time and labor are expended in the recurring rate contests, and some way should be found under legislative authority for arriving at results more promptly than is now possible under our present powers and practices."

The tenure of office (seven years) of the Commission should be materially increased, and their present compensation ($10,000 per annum) should be increased to a figure, commensurate with the labor and responsibility which the work entails.

The members of the Canadian Commission receive annual salaries of $15,000, and their appointments are for life. There cannot be the slightest doubt but that the labor and responsibility incident to a position on the Federal Commission is much greater than on the Canadian Commission, yet the members of our Commission receive less compensation, and are subject, every seven years, to the menace of non-reappointment.

(b) For the reasons heretofore given, the jurisdiction of the Interstate Commerce Commission should be specifically extended over all intra-state rates and practices affecting such rates.

(c) The Commission should be given specific jurisdiction* to prescribe minimum as well as maximum rates, as it is as much against public policy to

* For an example of the exercise by the Canadian Commission of its power to prevent reduction in rates, see in re Canadian Northern Ry. Company's Special Freight Tariff, Order No. 24727.

have unreasonably low rates* as it is to have unreasonably high rates.

(d) The Commission should be vested with the power, not to permit or prohibit the issuance of securities, but to require full publicity of such issues, and equal publicity as to the application of the proceeds thereof.†

The advantage of this plan, over that advocated of giving the Commission complete jurisdiction over the issuance of securities, is, that it will not substitute the discretion of the Government for that of the management of the railroad, as to the purpose for which the issue should be made, and will also remove the injurious delay, which in many instances, will necessarily result, if Governmental permission has to be had before the securities are issued.

That delay which would be inevitable, if the Commission were required to sanction the issue, would add to the cost of securing new capital, and, therefore, would be contrary to the public interest.

The publicity of the purposes of the issue, and of the application of the proceeds, will prevent the recurrence of such financial transactions, as have in the past, been deserving of severe criticism.

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* See opinion of Commissioner Harlan in Western Advance Rate Case, 35 I. C. C., at page 681.

† This conforms to the views expressed by the Railroad Securities Commission, of which President Hadley of Yale University was chairman, in their report to President Taft, under date of November 1, 1911.

(e) If jurisdiction over operating conditions is to be taken away from the States, it would probably be desirable to vest jurisdiction in the Federal Commission over certain operating matters, such as the number of the train crew, adequacy of signal protection, etc. It would not be possible, in this paper, to discuss the proper scope of this jurisdiction and its essential limitations.

Public policy demands that full jurisdiction be given to the Federal Commission over rates and practices affecting rates, but public policy also demands, that the freest latitude be accorded the operating departments of the Railroads, that is, to the men devoting their lives to the extremely technical questions of railroad operation.

Governmental control over operating conditions (by reason of their complexity, the necessity for knowledge of local conditions, and the importance of practical experience), is more likely to tend to inefficiency than to efficiency, though national control, through a Commission, is infinitely better than control through federal or state statute, or state commission.

(f) Jurisdiction should be vested in the Federal Commission to determine the reasonable rate to be paid by the Government for the transportation of the mail and parcels post, just as the Commission has today the power to determine the reasonable rate to be charged for the transportation of Governmental supplies and employees.

(g) Pooling Arrangements.

Carriers could be specifically permitted, subject to the approval of the Commission, to make traffic agreements which will secure the maintenance of reasonable rates, the elimination of discrimination, and the elimination of duplication of service, particularly in connection with the passenger service. It is highly probable, that economies in both freight and passenger transportation could be effected, by the elimination of the duplication of existing passenger service by different railroads between two cities, and by the pooling of freight traffic or earnings therefrom.

The prohibition in the Interstate Commerce Act against the pooling of traffic, is a relic of the idea, that the public interests were best served by competition. The underlying basis for that idea was that competition prevented unreasonably high rates and improved service. A regulatory body, such as a Commission, can secure these results without the necessity of competition. Unrestricted competition generally means waste, as is recognized by the decisions of many State Commissions, preventing the duplication of existing public utilities, and by the statutes of many States which require a certificate of public necessity before a proposed utility can even be incorporated.

(h) Power to suspend tariffs.

It seems to be a more or less general view that the Interstate Commerce Commission suspends all

tariffs making increases in rates. Such is not the fact, as will appear from an examination of the records of the Commission. At present the Commission has power to suspend tariffs for a maximum period of ten months, the result of which is that if a rate so suspended should subsequently be found to be reasonable, the carriers lose the revenue during the period in question, while if the rate had gone into effect and had subsequently been held to be unreasonable, the shipper would be entitled to reparation.

It is probable that there should be some modification with respect to the exercise of the power. Possibly it might with advantage be confined to cases involving questions of discrimination between localities, and be not exercised in cases which involve only the question of an advance in rates, unless there should be a more or less general advance, such as was involved in the Five Per cent. Case.

(i) The accounting requirements formulated by the Commission, the uniform demurrage rules,* the regulations for the transportation of explosives, and the bill of lading recommended by the Inter-

*The present condition of congestion on the eastern railroads, would seem to indicate the necessity of securing the co-operation of the Commission, towards increasing the demurrage charge, in cases where consignees are using freight cars for warehouses. See speech of George D. Dixon to the National Wholesale Lumber Dealers Association, March 16, 1916.

state Commerce Commission are a few examples* of the constructive work done by that body, and the people of the United States want more of work of that kind on the part of the Commission. Why should not our railroad legislation be as constructive as our banking and currency legislation? Why should not the Commission be given express authority to make recommendations to Congress and to the States, with respect to railroad legislation, present and prospective?

A Commission so empowered, might well call to the attention of the country, the growing burden of railroad taxation, state and national, and the economic injury inflicted thereby upon the country at large. The country needs, what Mr. Charles Francis Adams, the first Chairman of the Massachusetts Commission, designated as "the eventual supremacy of an enlightened public opinion," and the country looks to the Federal Commission, to secure such enlightenment on all railroad questions.

The effect of the present method of regulation on the revenues of the carriers.

The question may be asked: Has this conflicting, inefficient regulation injured the carriers, and consequently the general public? Yes, without the shadow of a doubt.

* See address by A. J. County before the Wharton School of the University of Pennsylvania.

Let me call your attention to the figures shown by the property investment and income accounts for the period 1900-1915,* of the Pennsylvania, New York Central, and Baltimore & Ohio Systems, the roads which the Commission regarded as typical of railroad conditions east of Chicago and north of the Potomac River.

In the case of the Pennsylvania System, the net operating income for 1915 was the lowest (with one exception, the year 1904) of any year since 1901, and in the fourteen years since 1901, the property investment had increased 650 millions of dollars; that is, roughly speaking, this amount of investment has earned nothing.

The year 1915 was not extraordinary; 1914 was almost as bad, it furnishing the lowest (with two exceptions) net operating income since 1901. In 1913, the year of largest returns, where the total operating revenue was 38 millions of dollars higher than in any previous year, the return on the property investment was lower than in any previous year.

As Mr. Rea pointed out in his testimony in the Five Per cent. Case, the Pennsylvania System, in a year which was the largest in its history, so far as traffic was concerned, with a larger amount of capital obligations oustanding than ever before, with a plant larger, more complete, and more efficient than at any time, finds itself no better off, so far as

* Fiscal years ending June 30th.

its owners are concerned, than it was fifteen years ago, when the country was just emerging from a period of financial, commercial and industrial depression, at least as severe, as any recorded.

If we were to examine the figures of the New York Central and the Baltimore & Ohio, we would find the same general facts therein and tendencies disclosed thereby, as in the case of the Pennsylvania System, and it was these facts which led Mr. Willard, the President of the Baltimore & Ohio, to say to the Commission on November 23, 1913, in his opening speech in the Five Per cent. Case:

> "I have shown that tendencies, which have been operating over a period of at least ten years, have resulted in such diminishing net returns that it has gradually come about that money invested in these railroads, because of the low average rates prevailing in so-called Official Classification Territory, and for other reasons, does not earn the same return as money invested in other enterprises of similar kind or character. As a matter of fact money so invested during the last three years, taken as a whole, has earned no return whatever. In view of all this, those responsible for the management of these properties would not be justified in continuing large expenditures of new capital for additional facilities and equipment, even if such capital were available at reasonable rates of interest."

These views were expressly confirmed by the Commission by their finding in the Five Per cent. Case, (31 I. C. C., at page 384):

> "That the net operating income of the railroads in Official Classification Territory,* taken as a whole, is smaller than is demanded in the interest of both the general public and the railroads."†

As a necessary result of the financial condition which has just been described, we find that comparing the five calendar years ending 1914 with the five calendar years ending 1910, the latter period shows a decrease, as compared with the former, of 42 per cent. in new mileage built, 32 per cent. in freight cars ordered, 29 per cent. in locomotives ordered, with an increase of 4½% in passenger cars ordered.‡

Railroad improvement has come to a standstill, for, as Mr. Rea said in his speech before the New York Chamber of Commerce:

> "Apparently the interests of everyone have been safe-guarded under public regulation except the interests of those who furnish the money for the public service; and we must protect these investors upon whom we must rely for future capital. Failure in the last

* This condition is not peculiar to the eastern roads. See Western Advance Rate Case, 35 I. C. C. 497.

† There will be a substantial improvement in the figures for the year ending June 30, 1916.

‡ Article by Mr. S. O. Dunn in the *North American Review* for November, 1915.

decade to protect the railroads and railroad investors has at last produced a lack of confidence in public regulation, and we now know that through the weakness of the railroads, the whole country is suffering."

Does anyone suppose that the public interests permit railroad development to stop? With 250,000 miles of main track, are we content with only 27,604 miles of second track? Are we to stop building and enlarging classification yards, installing automatic signals, removing grade crossings, constructing steel cars?* Yet that is what will happen under our present system of regulation, if we are to look to private capital for the development of our railway facilities; and a very slight experience of governmental operation of railroads in the United States, will confirm Mr. Acworth's statement, that no country has ever accepted government ownership because it was more desirable as an abstract proposition, but have only done so for military reasons, inability to secure private capital,† etc.

FEDERAL VALUATION OF RAILROADS

No discussion of the subject of governmental regulation of railroads would be complete, without a

* As to the importance of our railway system in connection with the question of national preparedness, see speech by George D. Dixon before the International Trade Congress on December 6, 1915.

† See "The Relation of Railroads to the State," by W. M. Acworth, 1914.

reference* to the valuation of all the property owned or used by common carriers subject to the provision of the Interstate Commerce Act, which is now being undertaken by the Interstate Commerce Commission pursuant to the provisions of the Act of Congress of March 1, 1913. The Act provides in substance that the Commission shall ascertain and report:

The value of all the property owned or used by every common carrier subject to the provisions of this Act.

The original cost to date, cost of reproduction new, and cost of reproduction less depreciation, of each piece of property owned or used by said common carrier, for its purposes as a common carrier.

The original cost, and present value, of all lands, rights of way, and terminals owned or used for the purpose of a common carrier.

The original cost, and present value, of property held for purposes, other than those of a common carrier.

Financial history of the Carrier—increases or decreases of stocks, etc.,—syndicate and other financial arrangements—net and gross earnings—expenditure of all moneys and the purposes for which the same were expended.

* For a thorough discussion of the valuation work, see articles by C. A. Prouty and Thomas W. Hulme (General Secretary of the President's Conference Committee) in the Annals of the American Academy of Political and Social Science for January, 1916, as well as an address delivered before the Traffic Club of Chicago on February 29, 1916, by Pierce Butler, of Counsel for the President's Conference Committee.

Amount and value of any aid, gift, grant, right of way, or donation made to any common carrier by any government or by individuals; value of land grants and concessions made by the carrier in exchange therefor.

It has been frequently stated that the valuation is only to be used for the purpose of fixing rates. If this were so, the question might well arise as to the wisdom of expending the enormous sum of money (fifty millions* or more) which the work will cost, in view of the few rate cases in which the valuation figures will be of importance.

If you will examine the thousands of decisions which the Federal Commission has handed down, you will find, in how few instances, the question of the valuation of the property of the carriers, is of any importance in that connection. The railroad rate structure of the country has been a matter of continual growth and development, primarily based upon the commercial necessities of each service, and rates, accordingly, are generally based, upon the value of the service, and not upon the cost of the service, or the value of the property employed therein. Of course, there are instances, involving a general advance in rates, as in the recent Five Per cent. Case and Western Rate Advance Case, and also cases where the carriers claim that their property is confiscated under rates fixed by Federal or State authority, in which the value of such property becomes of great importance.

* See article by Mr. Hulme, before referred to.

The Valuation Act is itself silent as to the purposes for which the valuation is to be used, though it states, that all final valuations fixed by the Commission shall be "*prima facie* evidence of the value of the property" in all proceedings under the Interstate Commerce Act, in judicial proceedings to enforce that Act, and in judicial proceedings to enjoin orders of the Commission.

That the purpose of the Valuation Act is not merely an incident of rate regulation, will be seen from the recommendations of the Commission on the subject (which doubtless were the potent reason for the enactment), as made from time to time, for twenty-five years prior to the passage of the Act. The Commission recommended that a valuation should be made for these purposes:

(1) To obtain a trustworthy estimate of the relation existing between the present worth of railroad property and its cost to its proprietors.

(2) In determining whether rates as fixed by the Government are confiscatory.

(3) In connection with railway taxation.

(4) In the ascertainment of a proper depreciation reserve.

(5) In testing the accuracy of the balance sheets of the carriers; and in the organization of railway statistics in general.

(6) In determining whether the railroads are under or over-capitalized.

The people of the United States are fortunate in having been able to secure the services of Mr. C. A. Prouty as Director of the Valuation Division organized by the Commission, his many years of experience as a member of that Commission making him peculiarly fitted to be in charge of this responsible work.

The Government is at present surveying about 4000 miles of road a month and expect to complete the work by approximately January 1, 1920.

The Rail Carriers have appointed Committees of engineering, land, equipment, accounting officers, as well as counsel, for the purpose of accomplishing the duty of co-operating with the Government, which the Act specifically requires.

Some idea may be obtained of the magnitude of the valuation work, when you consider that the Commission is required to ascertain not only the present value of 376,000 miles of tracks and sidings, but the value also of thousands of acres of land used for terminals, as well as the value of the securities and all other kinds of property owned by the carriers. The Commission is also required to ascertain the original cost to date, cost of reproduction new, and cost of reproduction less depreciation, of each piece of property, owned or used by the carriers, for their purposes as common carriers.

To find the cost of reproduction new, requires the ascertainment of grading quantities, their yardage and classification, a determination of questions of shrinkage and subsidence, the form and manner in which the road shall be reproduced, and the time required to reproduce the same. It requires also the ascertainment of engineering charges, contingencies, interest during construction, taxes, amounts to be allotted to promotion organization and administration, materials on hand, and working capital, as well as the determination of the unit prices to be applied to the quantities so ascertained.

In determining reproduction less depreciation, the Commission will be required to ascertain not only the extent and amount of depreciation, but also the extent and amount of appreciation, and finally there will come the ascertainment of the intangible values, which the Act designates as "other values and elements of value," such as location, going concern, etc.

Amongst the details, which the Act requires the Commission to ascertain, is the original cost to date of "each piece of property owned or used by said common carrier for its purposes as a common carrier." Though it may be possible to obtain the purchase price of a piece of property, it will be impossible, in many instances, to allocate to such piece of property the appropriate overhead charges and the cost of putting the property in place, all

of which are necessary elements in determining the cost to date of that piece of property. The records of the carriers have never been required to be kept so as to show the cost to date of each piece of property, and the attempt to ascertain the same, would probably involve a minimum expenditure of 50 millions of dollars.*

This brief outline of the magnitude of the valuation work will show how difficult, if not impossible, it is for a Commission of only seven members, with its manifold other duties, to give the time to the valuation work, which the importance of the subject demands.

Before leaving the subject of valuation, it may be of interest to know the position of such of the State Commissions as were represented at the recent argument before the Interstate Commerce Commission, on certain questions arising under the Valuation Act.

They contended, in substance, that the Interstate Commerce Commission should not ascertain the value of the property of the carriers, but should ascertain simply the three cost figures and other detail required by the Act, and leave for the future, when some rate case arises, the determination of some amount, which the Commission, in its then

* See Address of Director Prouty before the National Association of Railway Commissioners, 1914, page 140 of the proceedings.

judgment, should fix as a proper basis for rate regulation.

An attempt has been made in this paper to outline the present system of railroad regulation, its inherent defects, and to suggest for consideration certain remedies.

Certainly there is no question before us to-day which more vitally affects the economic development of the United States.